

**REPORT OF THE AUDITOR-GENERAL TO THE LIMPOPO PROVINCIAL LEGISLATURE
AND THE COUNCIL ON ELIAS MOTSOLEDI LOCAL MUNICIPALITY**

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of the Elias Motsoaledi Local Municipality, which comprise the statement of financial position as at 30 June 2011, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory information and the accounting officer's report as set out on pages xx to xx

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), and for such internal control as management determines necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of South Africa and section 4 of the Public Audit Act of South Africa, my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General notice 1111 of 2010* issued in *Government Gazette 33872 of 15 December 2010*. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer opinion

Accumulated surplus

4. Standards of Generally Recognised Accounting Practice, GRAP 3, *Accounting policies, changes in accounting estimates and errors* requires that an entity shall disclose the nature of the prior period error for each prior period presented, to the extent practicable, the amount of the correction for each financial statement line item affected; the amount of the correction at the beginning of the earliest prior period presented; and if retrospective restatement is impracticable for a particular prior period, the circumstances that led to the existence of that condition and a description of how and from when the error has been



corrected. The statement of changes in net assets includes corrections of prior period errors amounting to R57 068 981 (2010: R53 442 161) which were processed against the accumulated surplus balance of R1 019 000 612 (2010: R943 827 107). The content of this amount has not been properly disaggregated in note 37 to the annual financial statements. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that all corrections were properly recorded. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the existence, completeness, valuation and allocation of and obligation pertaining to the corrections.

Biological assets

5. Standards of Generally Recognised Accounting Practice, GRAP101, *Agriculture*, requires that biological assets to be disclosed in the financial statements. Biological assets are defined as living animals and plants. The municipality did not disclose game that belongs to them in the financial statements. The municipality's records did not permit the application of alternative audit procedures and consequently I was unable to satisfy myself as to the completeness, valuation and allocation of biological assets.

Commitments

6. Commitments as disclosed in note 32 to the financial statements excludes an amount of R7 353 910 identified from the municipality's contract management system. Commitments of R7 716 804, as stated in note 34 to the financial statements is understated by R7 353 910.

Expenditure

7. The municipality could not provide sufficient appropriate audit evidence to support journal entries of R3 455 076 debited and R1 041 103 credited to expenditure. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, accuracy, existence and classification of expenditure.

Other financial liabilities (Lease)

8. The other financial liabilities balance of R2 764 323 (2010: R2 786 004), as disclosed in note 12 to the financial statements, does not agree to the balance of R1 308 744 (2010: R1 506 166) per the finance lease register. The entity did not reconcile the difference of R1 455 579 (2010: R1 279 838) between the financial statements and the underlying accounting records. Consequently, the other financial liabilities balance is overstated by R1 455 579 (2010: R1 279 838). I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.
9. The municipality did not disclose separately the current and non-current portion of finance lease liabilities in accordance with the Standards of Generally Recognised Accounting

Practice, GRAP1, *Presentation of financial statements*, which states that for each liability line item that combines amounts expected to be recovered or settled within (a) no more than twelve months after the reporting date; and (b) more than twelve months after the reporting date, an entity shall disclose the amount expected to be recovered or settled after more than twelve months. Had this been done, current liabilities would have been stated in the statement of financial position at R617 483 (2010: R252 578) and other financial liabilities would have been reduced by the same amounts.

Investment property

10. The investment property register could not be provided for audit purposes, I was therefore unable to verify the completeness, valuation and allocation and existence of investment property amounting to R17 927 400 (2010: R17 927 400) as stated in note 2 to the financial statements.
11. The entity did not determine the fair value of investment property accounted for under the fair value model, in accordance with Standards of Generally Recognised Accounting Practice, GRAP 16, *Investment property*. Consequently, I could not satisfy myself as to the valuation and allocation of investment property.

Property, plant and equipment

12. Comparative figures as disclosed in note 3 to the financial statements include unexplained differences between prior year audited financial statements and the financial records of the municipality at R37 850 790. This difference could not be reconciled to the restatement of corresponding figures as disclosed in note 37 to the financial statements. No alternative audit procedures were possible and consequently I could not determine whether property, plant and equipment amounting to R565 592 848 disclosed in the annual financial statements as comparative figures, are complete and correctly valued and allocated.
13. Land identified from the valuation roll amounting to R58 148 918 (2010: R4 248 300) could not be traced to the fixed asset register. The municipality's records did not permit the application of alternative audit procedures and consequently I could not satisfy myself as to the completeness and valuation and allocation pertaining to land of the current and prior period.
14. Leased assets of R4 543 683 (2010: R3 902 763) disclosed in the fixed asset register is not separately identifiable or disaggregated into separate asset items. As a result I was unable to confirm the existence and completeness of leased assets amounting to R4 543 683 (2010: R3 902 763).
15. The municipality did not depreciate property, plant and equipment in accordance with the accounting policy adopted by the municipality. The depreciation rate as per the accounting policy differs from the depreciation rate used in calculating the depreciation charge for the

year. The amount of the misstatement cannot be quantified. Consequently, I was unable to satisfy myself as to the valuation and allocation of property, plant and equipment.

16. I have recalculated the accumulated depreciation for property, plant and equipment and noted a difference of R42 834 761. Accumulated depreciation as disclosed in note 4 to the financial statements is overstated by R42 834 761 and accumulated surplus is understated with the same amount.
17. The entity did not review the residual values and useful lives of property, plant and equipment at each reporting date in accordance with Standards of Generally Recognised Accounting Practice, GRAP 17, *Property, plant and equipment*. The municipality's records did not permit the application of alternative audit procedures. Consequently, the impact on the carrying value of property, plant and equipment and the corresponding effect on accumulated surplus in terms of GRAP 3 - *Accounting policies, changes in accounting estimates and errors* as disclosed in the statement of financial position could not be determined.
18. The Standards of Generally Recognised Accounting Practice, GRAP17, *Property, plant and equipment*, requires items of *property, plant and equipment* to be recognised at the acquisition cost (historical cost) or deemed cost where historical information is not available. Not all assets included in the asset register were unbundled and deemed cost at measurement date was not determined for all items of property, plant and equipment. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the valuation of property, plant and equipment.
19. Property, plant and equipment as disclosed in note 3 to the annual financial statements include an unexplained difference between the trial balance and the financial statements of R21 387 878. The municipality did not reconcile the difference of R21 387 878 between the financial statements and the underlying records. Consequently, property, plant and equipment is overstated by R21 387 878. I could not determine the effect on the other account balances or classes of transactions contained in the financial statements.
20. I was unable to verify the completeness and existence of property, plant and equipment, stated at R648 579 414 in note 4 to the financial statements as the assets were not allocated a unique asset number. The description and recording of property, plant and equipment in the accounting records of the municipality did not permit the application of alternative audit procedures regarding the completeness and existence of property, plant and equipment.
21. The municipality could not provide sufficient appropriate audit evidence to support journal entries of R2 576 903 debited and R2 362 057 credited to property, plant and equipment. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to

the completeness and valuation of property, plant and equipment.

Provision for bad debts

22. Included in accounts receivable is an amount of R78 797, the recovery of which is doubtful, based on the past payment history of the specific debtor. An impairment loss has not been recognised in accordance with South African Statements of Generally Accepted Accounting Practice, IAS 39 (AC 133), *Financial instruments: Recognition and measurement*. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of the provision for bad debts.

Revenue

23. There was no system of control over property rates revenue on which I could rely for the purpose of my audit, and there were no satisfactory procedures that I could perform to obtain reasonable assurance that all property rates revenue was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of property rates revenue recognised at R10 705 580 (2010: R10 735 965), as disclosed in note 18 to the financial statements.
24. There was no system of control over revenue derived from rental of municipal buildings on which I could rely on for the purpose of my audit, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that all rental income was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of rental income of R683 186 (2010: R1 328 837).
25. The municipality could not provide sufficient appropriate audit evidence to support journal entries of R2 152 293 credited to revenue and R600 240 and R1 552 053 debited to unspent conditional grant liabilities and trade payables respectively. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, accuracy, existence and classification of revenue.

Trade and other payables

26. My audit report for the prior year dated 30 November 2010 was modified due to:
- Figures disclosed in the financial statements which included unexplained differences between the audited financial statements and the financial records of the municipality of R5 982 756. These differences could not be reconciled to the restatement of corresponding figures as disclosed in note 37 to the financial statements. No alternative audit procedures were possible and consequently I could not determine whether trade payables amounting to R6 888 258 disclosed in note 15 to the annual financial statements as comparative figures, are correctly disclosed.

- Suspense accounts for unallocated deposits and expenses not captured in the cashbook amounting to R1 733 239 and R1 346 352 respectively with no reconciliations provided. The municipality's records did not permit the application of alternative audit procedures regarding the clearing of these suspense accounts.
- This has not been adequately resolved in the current year, and I am unable to determine the impact, if any, on the prior year's accumulated surplus.

27. Treasury Regulation 17.1.2 requires the sources of the transactions in a clearing account to be readily identifiable and monthly reconciliations to be performed to confirm the balance of the account. This information could not be provided for the accounts payable clearing account balance of R504 455, included in trade payables of R5 393 399 as disclosed in note 15 to the financial statements. The entity's records did not permit the application of alternative audit procedures regarding the accounts payable clearing account. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the existence, completeness, valuation and allocation of and obligations pertaining to the accounts payable clearing account balance.

28. A correction of R1 733 239 was made to accumulated surplus regarding the clearing of suspense accounts, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the existence, completeness, valuation and allocation of and obligation pertaining to the correction.

29. Retention creditors of R6 988 348 as disclosed in note 17 to the annual financial statements, excludes an amount of R1 733 207 identified from the municipality's contract management system. Retention creditors and property, plant and equipment is understated by R1 733 207.

Trade and other receivables

30. My audit report for the prior year dated 30 November 2010 was modified due to an unexplained difference between the audited financial statements and the financial records of the municipality of R557 644. The municipality did not reconcile the difference between the financial statements and the underlying accounting records. This has not been adequately resolved in the current year and consequently I could not determine whether trade and other receivables amounting to R455 601 971 as disclosed in note 8 to the annual financial statements as comparative figures, are correctly disclosed.

31. The municipality could not provide sufficient appropriate audit evidence to support journal entries of R275 852 debited and R30 028 818 credited to trade and other receivables. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of trade and other receivables stated at R425 181 111 in

note 6 to the financial statements.

32. The municipality could not provide sufficient appropriate audit evidence to support journal entries of R6 172 740 debited and R8 219 907 credited to VAT receivables. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of VAT receivables stated at R4 974 911 in note 7 to the financial statements.

Unspent conditional grants

33. My audit report for the prior year dated 30 November 2010 was modified due to an unexplained difference of R1 584 509 between the audited financial statements and the financial records of the municipality. The municipality did not reconcile the difference between the financial statements and the underlying accounting records. This has not been adequately resolved in the current year and consequently I could not determine whether unspent conditional grant liabilities amounting to R693 298 as disclosed in note 13 to the annual financial statements as comparative figures, are correctly disclosed.

Unauthorised expenditure

34. The municipality incurred unauthorised expenditure of R10 886 830 as a result of exceeding the total amount appropriated for a vote in the approved budget. The amount was not disclosed in a note to the financial statements, resulting in unauthorised expenditure being understated by R10 886 830.

Irregular expenditure

35. Section 125(2)(d) of the MFMA requires a municipality to disclose particulars of any material losses and material irregular, fruitless and wasteful and unauthorised expenditure that occurred during the financial year and whether these are recoverable. Expenditure amounting to R4 123 588 were incurred in contravention of the supply chain management and Municipal Systems Act requirements and the preferential procurement policy framework act. The amount was not disclosed in the financial statements resulting in irregular expenditure being understated by R4 123 588.
36. No system was in place for the identification and recognition of irregular expenditure and there were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that all irregular expenditure was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of irregular expenditure of R172 293 as disclosed in note 43 to the financial statements.

Cash flow statement

37. Presentation of a cash flow statement, summarising the entity's operating, investing and financing activities is required by the Standard of Generally Recognised Accounting Practice, GRAP 2: *Cash flow statements*. The following material unexplained and irreconcilable differences were identified:

- Cash received from sale of goods and services and grants of R180 431 479 is overstated with an amount of R33 278 026;
- Cash paid to suppliers and employees of R98 864 625 is understated with an amount of R33 278 018.
- Cash and cash equivalents at end of period is understated with an amount of R37 699.

38. The comparative figures could not be verified as 2009 comparative information has been restated without disclosing the restatement as required by Standards of Generally Recognised Accounting Practice, GRAP 3, *Accounting policies, changes in accounting estimates and errors*.

Basis of disclaimer

39. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matter

I draw attention to the matters below. My opinion is not modified in respect of these matters:

Restatement of corresponding figures

40. As disclosed in note 37 to the financial statements, the corresponding figures for 30 June 2010 have been restated as a result of an error discovered during 2011 in the financial statements of the municipality at, and for the year ended, 30 June 2010

Additional matter

I draw attention to the matter below. My opinion is not modified in respect of this matter:

Unaudited supplementary schedules

41. The supplementary information set out on pages X to X does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

42. In accordance with the PAA and in terms of General notice 1111 of 2010, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages XXX to XXX and material non-compliance with laws and regulations applicable to the municipality

Predetermined objectives

Usefulness of information

43. The reported performance information was deficient in respect of the following criteria:

- **Consistency:** The reported objectives, indicators and targets are not consistent with the approved integrated development plan.
- **Relevance:** There is no clear and logical link between the objectives, outcomes, outputs, indicators and performance targets.
- **Measurability:** The indicators are not well defined and/or verifiable, and targets are not specific, measurable, and time bound.

The following audit findings relate to the above criteria:

44. Reported performance against predetermined objectives is not consistent with the approved integrated development plan.
45. Approved targets of the municipality were found not to be well defined and verifiable, and targets are not specific and measurable.

Reliability of information

46. The reported performance information was deficient in respect of the following criteria:

- **Validity:** The reported performance did not occur and does not pertain to the entity.
- **Accuracy:** The amounts, numbers and other data relating to reported actual performance have not been substantiated by sufficient and appropriate audit evidence.
- **Completeness:** All actual results and events that should have been recorded have not been included in the reported performance information.

The following audit findings relate to the above criteria:

47. Relevant supporting documentation for the actual results achieved in the annual performance report could not be provided.
48. Reported actual performance information differs from the municipality's underlying records.
49. The actual achievements of all planned objectives specified in the service delivery budget implementation plan for the year under review were not included in the report on predetermined objectives submitted for audit purposes.

Compliance with laws and regulations

Budgets

50. The municipality incurred expenditure that was in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.

Annual financial statements, performance and annual report

51. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of current assets, current liabilities and disclosure items identified by the auditors were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a disclaimer audit opinion.

Conditional grants

52. Sufficient appropriate audit evidence could not be obtained that the allocations for Finance Management Grant and Municipal Systems Improvement Grant were utilised for the purposes stipulated in their respective schedules or Gazetted Division of Revenue Act framework, as required by section 15(1) of the Division of Revenue Act.

Internal audit

53. The municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes as required by section 45(1)(a) of the MSA and Municipal planning and performance management regulation 14.

Audit committees

54. No audit committee was in place as required by section 166(1) of the MFMA.

Procurement and contract management

55. Goods and service with a transaction value of between R10 000 and R200 000 were procured without obtaining written price quotations from at least three different prospective providers as per the requirements of SCM regulation 17(a) and (c).
56. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids as per the requirements of SCM regulation 19(a) and 36(1).
57. Invitations for competitive bidding were not always advertised for a required minimum period of days as per the requirements of SCM regulation 22(1) and 22(2).
58. Awards were made to providers who are persons in service of other state institutions in contravention of the requirements of SCM regulations 44. Furthermore the provider failed to declare that he / she is in the service of the state as required by SCM regulation 13(c).

Expenditure management

59. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
60. The accounting officer did not take reasonable steps to prevent unauthorised, irregular expenditure, fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Revenue management

61. Revenue received by the municipality was not always reconciled at least on a weekly basis, as required by section 64(2)(h) of the MFMA.

Asset management

62. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained an effective system of internal control for assets (including an asset register) as required by section 63(2)(c) of the MFMA.

INTERNAL CONTROL

63. In accordance with the PAA and in terms of General notice 1111 of 2010, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report

Leadership

- The municipality did not have sufficient monitoring controls in place resulting in materially incorrect financial statements submitted for audit purposes. No review of the annual financial statements resulted in material adjustments to the annual financial statements and report on predetermined objectives.

Financial and performance management

- Annual financial statements submitted required numerous significant amendments as a result of a lack of understanding the applicable reporting framework standards.

Governance

- An audit committee was not established during the year under review.

Auditor General

Polokwane

30 November 2011



**AUDITOR - GENERAL
SOUTH AFRICA**

Auditing to build public confidence